

IDAHO LOTTERY



STRATEGIC PLAN

FISCAL YEARS 2005-2008

Submitted this 1st day of July 2004

A handwritten signature in black ink, appearing to read "Roger D. Simmons".

Roger D. Simmons, Director

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SECTION I

**ORGANIZATION AND OPERATION
OF THE LOTTERY**

I. ORGANIZATION AND OPERATION OF THE LOTTERY

A. ORGANIZATION

The Idaho State Lottery, doing business as the Idaho Lottery, is established by Chapter 74, *Idaho Code*, for the purpose of operating the state lottery at the least public expense and the smallest staffing possible. Organizationally the Idaho Lottery is located within the Department of self-governing Agencies. The Lottery is organized into four divisions; Administration, Information Systems, Sales & Marketing, and Security. An organizational chart is included as Appendix A.

Lottery tickets are sold through contracted lottery retailers, primarily convenience stores, supermarkets, etc. The retailers receive 5% of sales as a base commission. They also can earn additional payments in the form of sales and cashing bonuses. The total for such additional payments is limited to a statewide total of 1% of sales. There are approximately 1000 retailers statewide. As of this update there are 735 selling both scratch and lotto tickets, 185 are selling only scratch tickets and 208 selling only pulltabs. These numbers fluctuate weekly as field sales representatives recruit new outlets or as ownership changes and retailers are dropped from the current lottery sales force.

A critical element to the success of our efforts is our relationship with our three major vendor-partners, GTECH (lotto gaming services), Oberthur Gaming Technologies-OGT (scratch tickets), and es/Drake (advertising). The GTECH basic contract terminates February 28, 2006. The OGT contract September 30, 2007, while the es/Drake contract ends on June 30, 2007.

Two of our three Lotto Games (Powerball and Wild Card II) are operated in association with some or all of our partners in the Multi-State Lottery Association (MUSL). MUSL is a non-profit, government-benefit association owned and operated by its 30 member lotteries. Each MUSL member offers one or more of the games administered by MUSL. All profits are retained by the state lottery and are used to fund projects approved by the state legislatures.

The current MUSL members are: Arizona Lottery, California Lottery, Connecticut Lottery Corporation, Colorado Lottery, D.C. Lottery and Charitable Games Control Board, Delaware State Lottery, Hoosier Lottery, Idaho Lottery, Iowa Lottery, Kansas Lottery, Kentucky Lottery Corporation, Louisiana Lottery Corporation, Maine Lottery, Minnesota State Lottery, Missouri Lottery, Montana Lottery, Nebraska Lottery, New Hampshire Sweepstakes Commission, New Mexico Lottery Authority, North Dakota Lottery, Oregon Lottery, Pennsylvania Lottery, Rhode Island Lottery, South Carolina Education Lottery, South Dakota Lottery, Tennessee Educational Lottery, Vermont Lottery, Virgin Islands, Wisconsin Lottery, West Virginia Lottery.

B. REVENUES

More than 99-and-a-half per-cent of Lottery revenues are derived from the sale of Lottery tickets. The remaining revenue, classified as “other income” on the income statements is derived from interest earnings on our prize reserve accounts, and from license fees. Lottery sales fall into two major classifications, Scratch/pull-tab tickets which account for approximately 63% of sales and lotto tickets which account for the remaining 37% of sales. These two classes can be further divided by lottery products or games.

1.Scratch Tickets

- (a) **Scratch tickets** are approximately 62% of total sales. These tickets sell from \$1 to \$15 each and have a pre-printed play area covered with latex which is scratched off to reveal if it is a winning ticket and if so the amount of the prize. Cash prizes range from \$1 to \$150,000.
- (b) **Pull-tab tickets** are approximately 1% of total sales. Pull-tab tickets sell from \$.25 to \$1 each like scratch tickets and have a pre-printed play area. The play area is revealed by peeling back a series of covering tabs, consequently the term “pull-tab”. Prizes range from \$.25 to \$500. Pull-tabs are designed to be played primarily in bar and restaurant settings.

2.Lotto.

Lotto tickets are sold through a lottery terminal located at approximately 735 retailer locations throughout the state and are connected by satellite to a central computer located in Lottery headquarters. Players pick a series of numbers and these numbers, along with the ticket number are recorded on the central computer. Currently, the Idaho Lottery offers three separate lotto-style games. Powerball and Wild Card are multi-state games. Pick Three is offered only to Idaho players. Twice a week televised drawings are held to determine the winning numbers for Powerball. Players holding tickets with all winning numbers win all or a share of the “jackpot” (top prize) for that draw. In the event the jackpot is not won, it becomes part of the jackpot for the next drawing. It is not uncommon to have large, growing jackpots because there was not a winner for several draws.

With the growth in the jackpot amount, there is normally a corresponding increase in the level of sales. In addition to the jackpot, lesser prizes are awarded for selecting some, but not all, of the numbers.

As mentioned previously, Idaho currently offers three different lotto games. Each game has different odds and a different jackpot level. These differences distinguish the games and consequently their appeal to different segments of the player base. The games are as follows:

- (a) **Powerball-** approximately 33% of total sales for fiscal year 2005. Average jackpot of approximately \$88,000,000. Played in conjunction with a MUSL group consisting of 27 other states and the District of Columbia and the U.S. Virgin Islands. Drawings are held Wednesdays and Saturdays.
- (b) **Wild Card II-** approximately 2.5% of total sales for fiscal year 2005. Average jackpot approximately \$1,000,000. Played in conjunction with Montana, North Dakota and South Dakota as part of MUSL. Drawings are held Wednesdays and Saturdays.
- (c) **Pick 3-** approximately 1.5 % of total sales for fiscal year 2005. Average winnings for a \$1 play is between \$50 and \$500. Drawings are held daily except Sundays.

C. EXPENSES AND CONTROLS

As a state agency, the Idaho Lottery is subject to most of the same administrative controls as other state agencies, including budgetary controls. The agency is authorized to expend funds in the following four areas (budget programs):

<i>*Administration-</i>	Includes personnel costs, ticket production costs, rent, telephone, equipment, etc.
<i>*Advertising/Promotion-</i>	Includes the cost of producing and running the advertising and promotions that support ticket sales.
<i>*Prize Expense-</i>	Prizes paid to lottery winners
<i>*Commissions:</i>	Commissions paid to retailers for selling tickets.

The annual appropriation for the administration program is “fixed”, i.e., it cannot be exceeded regardless of the number of tickets sold. The appropriations for the remaining three programs are “continuous” meaning that they can be increased if sales increase. There are spending limitations on these programs, however. Advertising and promotion expenditures cannot exceed 3.5% of revenues, and commissions cannot exceed 6% of revenues. There is a similar “cap” for administrative expenses; they may not exceed 15% of revenues. Currently, the fixed appropriation represents only about 11% of estimated revenues.

D. Dividends

Approximately \$.78 of each dollar of sales is used to fund expenses, with the remaining \$.22 available for the dividend. This is broken down as follows:

Sales Revenue:	\$1.00
Administration	\$.112
Advertising & Promotion	\$.033
Prizes	\$.580
Commissions	<u>\$.059</u>
TOTAL EXPENSES	<u>\$. 78</u>
Available for Dividends	\$.22

One-half of the annual dividend goes into the *Public School Building Fund* and is distributed to the various local school districts. The other half goes into the *Permanent Building Fund* for the construction and maintenance of public buildings. Since the Lottery's inception to date the following dividend payments have been made from the revenue generated in the fiscal year indicated:

FISCAL YEAR 1990	\$ 17,225,000
FISCAL YEAR 1991	\$ 17,225,000
FISCAL YEAR 1992	\$ 12,000,000
FISCAL YEAR 1993	\$ 14,000,000
FISCAL YEAR 1994	\$ 18,000,000
FISCAL YEAR 1995	\$ 19,000,000
FISCAL YEAR 1996	\$ 20,000,000
FISCAL YEAR 1997	\$ 19,500,000
FISCAL YEAR 1998	\$ 20,500,000
FISCAL YEAR 1999	\$ 20,600,000
FISCAL YEAR 2000	\$ 18,000,000
FISCAL YEAR 2001	\$ 15,000,000
FISCAL YEAR 2002	\$ 18,000,000
FISCAL YEAR 2003	\$ 20,500,000
FISCAL YEAR 2004	<u>\$ 25,000,000</u>
TOTAL	\$274,550,000

SECTION II
STRATEGIC PLAN

ISSUES/CHALLENGES

The Idaho Lottery is a public entity established for the public good. Some of the citizens of the State, however, object to the Lottery for various reasons. In pursuing our objective, we must be sensitive to this fact especially in the manner in which the Lottery is promoted. Section 67-7401, Idaho Code, requires “all advertising by the lottery shall be conducted in a manner consonant with the dignity of the state and the sensibilities of its citizens”.

Lottery purchases are made from player’s discretionary purchase options. Players must feel that the entertainment value they receive from Lottery products is worth the cost of those discretionary dollars or they shift those purchases elsewhere. In promotion, care has to be taken to emphasize the entertainment value plus the public good (at least 22 cents from every dollar of sales goes to public schools and buildings). While the publication of winners names is essential in demonstrating the “winability “ of lottery games, care has been taken to avoid promoting them as a method to “get rich quick”.

Scratch ticket purchases are generally made on impulse. The most important factors driving sales are product placement, i.e.; having the tickets prominently displaced near the cash register and “freshness”-a variety of new, entertaining games.

Lotto ticket purchases, while sometimes an impulse buy, are more likely to be the result of a planed purchase. The level of lotto sales is directly related to jackpot size; the higher the jackpot, the greater the sales. Consequently, Jackpot awareness is an essential element in marketing lotto games.

A key element in the success of the Lottery is the support of the approximately 1000 retailers throughout the state. Commissions on lottery sales are generally five-percent of sales, although additional amounts, up to one-percent of sales, can be allocated among the retailers for bonus and incentives.

While every effort must be made to increase revenue, dividend maximization will also require effect cost control measures.

MISSION STATEMENT:

The mission of the Idaho Lottery is to maximize net income and the resulting annual dividend payment for Idaho public schools and building

VISION STATEMENT:

We envision the Idaho Lottery providing a diverse mixture of entertaining lottery products through an efficient and innovative public enterprise built upon security and integrity and supported by an effective public/private partnership with our retailers. The Results of our efforts will be an ever-increasing annual dividend payment to help support Idaho public schools and buildings.

Goal:

Our goal for fiscal years 2005 through 2008, is to increase the annual dividend by at least \$500,000.

The dividend resulting from FY-2004 operations was \$25,000,000. However since much of the additional revenue was the result of an extraordinary number (five times in FY-2004 the Powerball jackpot exceeded \$100-million dollars) of high Powerball jackpots, Lottery Staff believes that a more conservative estimate should be used for future periods. Accordingly, dividend projections are as follows:

FY-2005	\$23.0 Million
FY-2006	\$23.5 Million
FY-2007	\$24.0 Million
FY-2008	\$24.5 Million

A schedule of our estimated results of operations is included as attachment B. This schedule incorporates the estimated revenues and expenses resulting from achieving our stated objectives as described in the following pages.

Objective 1- To obtain an annual lotto ticket sales growth of at least 1.5% for fiscal years 2005 through 2008.

STRATEGIES:

Increased Powerball sales as a result of changing the matrix. Powerball sales are clearly a factor of the announced jackpot. The higher the jackpot, the greater the sales. Over the previous two years, the addition of the Pennsylvania , South Carolina, Tennessee, North Dakota and U.S. Virgin Island lotteries to the Powerball group means greater sales, and thus higher jackpots. However, an increased player base also increased the probability that the jackpot will be won more frequently. Accordingly, effective with the start of sales on October 6, 2002, MUSL changed the Powerball matrix, i.e., the range of numbers selected, thereby increasing the odds of winning the jackpot. The increased player population combined with the matrix change did, in fact, increase the average jackpot with a resulting increase in sales. The Powerball matrix now has overall odds of 1 in 36 and an average jackpot of \$88 million.

While the MUSL group is continuing to seek new member lotteries, no expansion is expected in FY-2005. Similarly, no matrix change is anticipated. The expected growth in Idaho Lottery Powerball sales will be the result of increased growth in the State's population combined with increased marketing and promotion of the game.

Maintain sales of Wild Card II and Pick-3 Through FY-2008. Both *Wild Card II* and *Pick-3* have a solid, if predictable player base. While we will continue to cross-promote these games with our other lotto games, we do so with the expectation of merely maintaining or moderately increasing sales.

Continue to add additional lotto retailers. During the period we also hope to expand the number of locations where lotto tickets can be purchased thereby increasing over-all sales. This can be done by adding new retailers or by converting existing “scratch only” retailers to scratch and lotto ticket retailers. Since the present contract with GTECH provides for a finite number of terminals this expansion will likely be dependent upon negotiating a mutually beneficial agreement between the Lottery and GTECH.

ACTIONS:

The following actions are planned in support of our strategies for objective 1:

- Expand the present lotto retailer base of 735 to the following levels by June 30th of each of the following fiscal years:

FY-2005	735
FY-2006	745
FY-2007	755
FY-2008	765

Objective 2 To obtain an annual sales increase of at least 2% for scratch and pull-tab tickets for fiscal years 2005 through 2008.

STRATEGIES:

Continue to provide fresh entertaining scratch and pull-tab tickets. Scratch Ticket sales had been in a general decline since FY –1998, although FY-2002 saw a slight reversal of this trend. A sharp upward trend in scratch ticket sales was evident in FY-2003 and continued through FY-2004.

Part of the increase can be attributed to the fact that the Lottery offered a smaller percentage of \$1 games and more \$2 games, and an increasing number of \$3, \$5 and \$7 games. The \$15, 15th Anniversary ticket, for example, averaged more than a-quarter-million dollars in sales per week during its first 100 days on the market. In increasing the average “price-point” of the scratch tickets, The Lottery also offered many more play features to make the games more interesting and thus making them more entertaining to play.

This is a formula which appears to work and we will continue to improve upon it. In addition we will continue with our scratch ticket “winner awareness” campaign begun in FY-2003. This campaign carried out through television, print and point-of-sale advertising stresses the “winability” of the scratch ticket product..

Expand the use of scratch ticket vending machines. Wherever they have been placed, scratch ticket vending machines have increased sales of scratch tickets. The lottery presently has 220 machines placed. Our experience has been that these machines pay for themselves in less eight months. Our major concern with the vending machines is their possible use by under age players. We have attempted to guard against this possibility by requiring the vending machines be placed in a area clearly visible to store employees and providing signage warning minors that they must be 18 to purchase lottery tickets. Another issue involves the age of the vending machines currently in use in Idaho. Many of our machines were purchased almost a decade ago and maintenance on the older machines is increasing. Because we bought the machines, the Idaho Lottery will have to absorb any obsolescence. In the future, the Lottery should trend toward leasing instead of purchasing any equipment with a predicted short technological life span.

ACTIONS:

The following actions are planned in support of our strategies for objective 2.

- Add the following number of scratch ticket vending machines in each of the following fiscal year:

FY-2005	20
FY-2006	20
FY-2007	30

Objective 3 To improve general over-all operation of the Lottery by reducing costs thereby increasing the annual dividend.

STRATEGIES:

Find ways of reducing operating costs. The Lottery is constantly evaluating its operating costs in an effort to increase its annual dividend.

As an example, in February 2003, the Lottery extended its contract with its lotto vendor, GTECH. In return for extending the contract, GTECH provided, at no additional cost to the Lottery, a satellite and radio communications system, replacing the existing telephone only system. The Lottery has paid over \$1.2 million a year to the various private telephone companies throughout the state to support the existing telephone network. Conversion to the satellite and radio system will save the Lottery \$200,000 in FY-2005. The projected savings in subsequent fiscal years will be even more since the satellite/radio costs are fixed over the contract, while telephone costs would otherwise have continued to increase.

In addition, as part of the GTECH contract extension, GTECH provided 800 new state-of-the-art lotto terminals. Not only did the new terminals greatly improve our relations with our retailers, but it allow the Lottery to increase the number of lotto retailers from 724 to 735 without increasing its cost.

During FY-2003, the Lottery re-bid its contract for scratch tickets and accepted the bid of Oberthur Gaming Technologies-OGT to provide scratch tickets through September 30, 2007. Under the new contract, the Lottery will pay OGT based on a percentage of scratch tickets sold. Since the Lottery previously purchased the tickets outright and thus absorbed the cost of any unsold tickets, the new methodology has reduced costs by nearly \$300,000 in FY-2005.

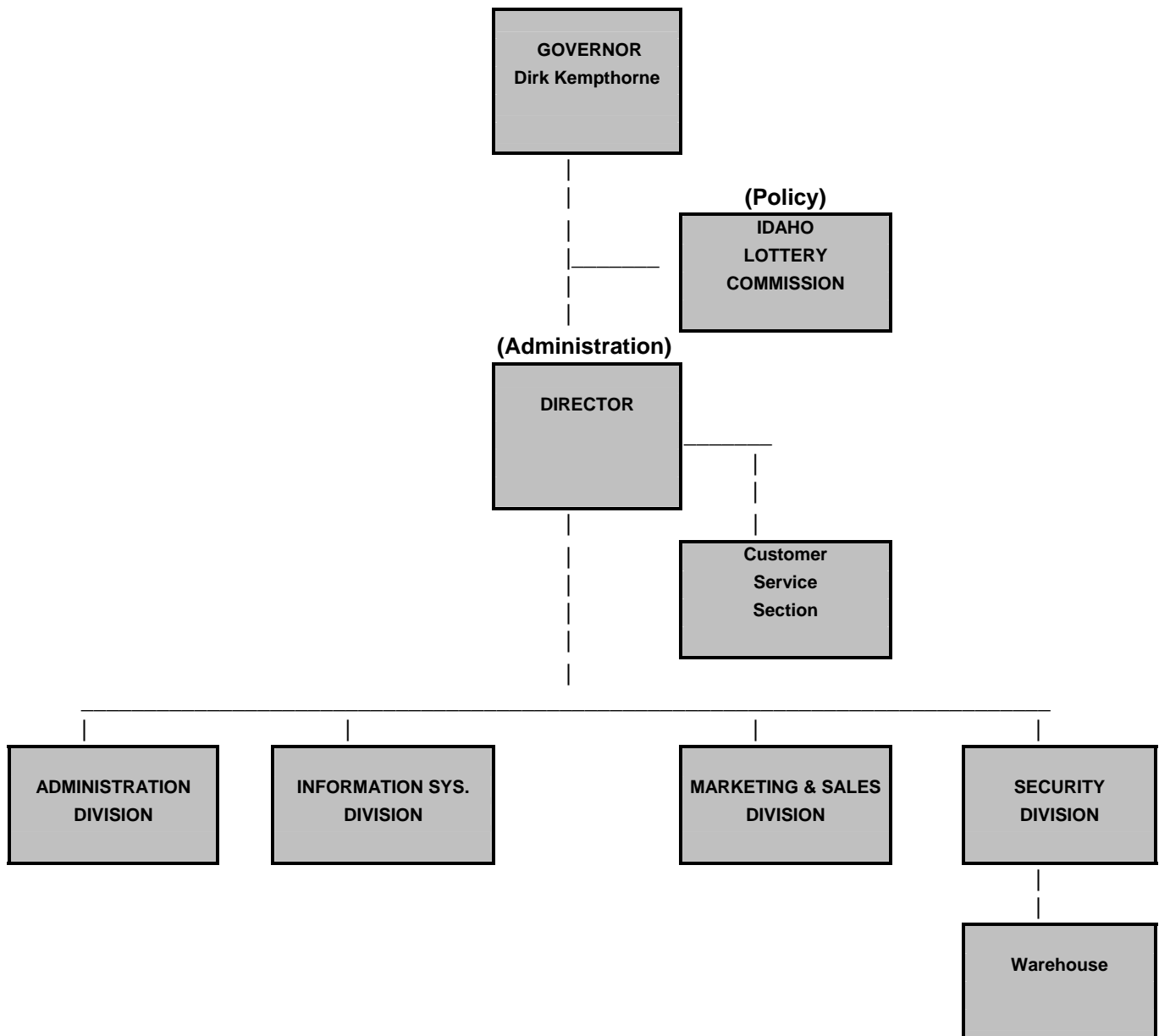
ACTIONS:

The following actions are planned in support of our strategies for objective 3:
Continue to find methods to cut cost and thereby increase profitability.

- Replace the present fleet of eleven four-year-old lottery vans with new, cleaner, more fuel efficient vans. Also install a global positioning system (GPS) tracking monitor in the vans in order to more effectively evaluate weekly routing and use.
- Reorganize and realign regional sales representative thereby eliminating a half-time position.

- Automate nightly computer processing, thereby eliminating a half-time operator position.
- Recruit and train senior volunteers to assist with promotions at fairs and other venues, thereby reducing the need for paid temporary employees and overtime for regular employees.

APPENDIX -A IDAHO LOTTERY ORGANIZATIONAL CHART



APPENDIX- B

PROJECTED RESULTS OF OPERATIONS

FISCAL YEARS 2005-2008

	FY-2005 PROJECTED	FY-2006 PROJECTED	FY-2007 PROJECTED	FY-2008 PROJECTED
Operating Revenues:				
Instant ticket sales	\$66,000,000	\$67,320,000	\$68,666,400	\$70,039,728
On-line ticket sales	36,000,000	36,540,000	37,088,100	37,644,422
Break-open instant ticket sales	1,000,000	1,020,000	1,040,400	1,061,208
TOTAL OPERATING REVENUES	103,000,000	104,880,000	106,794,900	108,745,358
Operating Expenses:				
Prizes	59,370,043	60,453,690	61,557,455	62,681,714
Retailer commissions	6,017,171	6,126,999	6,238,866	6,352,810
On-line games commissions	1,745,963	1,777,831	1,810,291	1,843,353
Instant tickets	1,880,100	1,914,416	1,949,370	1,984,972
Break open instant ticket costs	65,111	66,299	67,510	68,743
Advertising	3,120,814	3,177,776	3,235,796	3,294,893
Salaries and benefits	2,407,252	2,451,190	2,495,944	2,541,528
Telephone and data line costs*	752,107	765,835	779,817	794,060
Depreciation and amortization	1,683,872	1,500,000	1,400,000	1,200,000
Office and equipment	463,631	472,094	480,713	489,493
Shipping costs	423,632	431,364	439,240	447,262
Professional services	1,324,798	1,348,979	1,373,608	1,398,695
Supplies	143,371	145,988	148,653	151,368
On-line ticket promotions	0	0	0	0
Television production costs	170,906	174,026	177,203	180,439
Other	400,000	420,000	440,000	460,000
Interest				
TOTAL OPERATING EXPENSES	79,968,771	81,226,487	82,594,466	83,889,332
OPERATING INCOME	23,031,229	23,653,513	24,200,434	24,856,026